

BEFORE THE TAX COMMISSION OF THE STATE OF IDAHO

In the Matter of the Protest of

[Redacted]

Petitioners.

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DOCKET NO. 18238

DECISION

On July 16, 2004, the Idaho State Tax Commission's (Commission) Income Tax Audit Bureau (Bureau) issued a Notice of Deficiency Determination to [Redacted] ([Redacted]) for the taxable years 2000, 2001, and 2002. The adjustments proposed by the Bureau in its NODD did not result in any additional tax due since [Redacted] filed as an Idaho S corporation for tax years 2000 through 2002; however, the adjustments do have a tax impact to its shareholders, [Redacted].

On July 16, 2004, the Bureau issued a Notice of Deficiency Determination to [Redacted], proposing additional income tax and interest for the taxable years 2000, 2001, and 2002 in the total amount of \$13,996.

After receiving additional information, the Bureau issued a modified audit report to [Redacted] and to the [Redacted]. As a result of the modified audit reports, the amount of proposed additional income tax and interest for the taxable years 2000, 2001, and 2002, was reduced from \$13,996 to \$7,654.

On August 4, 2005, the Bureau issued a Notice of Deficiency Determination to [Redacted] for taxable year 2003. The adjustments proposed by the Bureau in its NODD did not result in any additional tax due since [Redacted] filed as an Idaho S corporation for tax year 2003; however, the adjustments do have a tax impact to its shareholders, [Redacted].

On August 4, 2005, the Bureau issued a Notice of Deficiency Determination to [Redacted], proposing additional income tax and interest for the taxable year 2003 in the total amount of \$2,348.

On August 10, 2004, the Bureau received a petition for redetermination on behalf of [Redacted] in response to the NODD issued by the Bureau on July 16, 2004, covering tax years 2000, 2001, and 2002, in which [Redacted] indicated additional information would be forthcoming. Additional information was provided and, as stated above, a modified audit report was issued on July 29, 2005, to [Redacted] and to the [Redacted]s incorporating the additional information.

On August 14, 2004, the Bureau acknowledged receiving the petition for redetermination filed on behalf of [Redacted] for tax years 2000 through 2002. The Commission is unable to locate any petition for redetermination filed on behalf of the [Redacted]s or [Redacted] for the 2003 tax year. Since [Redacted] and the [Redacted]s did not file a timely petition for redetermination regarding the Bureau's adjustments to [Redacted]'s and [Redacted]s' 2003 tax year, the timeframe for doing so has expired and, in accordance with Idaho Code section 63-3045(5), "the deficiency shall be assessed and shall become due and payable upon notice and demand from the state tax commission." Accordingly, the remainder of this Decision will focus strictly on the Notice of Deficiency issued to [Redacted] for tax years 2000 through 2002 and the corresponding Notice of Deficiency Determination issued to the [Redacted] for the same tax years both as modified by the Bureau on July 29, 2005.

The Commission issued its hearing rights letter to [Redacted] on January 3, 2006, informing [Redacted] of its appeals rights for tax years 2000 through 2002 and subsequently followed up its hearing rights letter with two phone calls. To date the Commission has not

received a request for a hearing and hereby issues its decision based upon the information available.

[Redacted]. ([Redacted])

In the Bureau's Modified Audit Report for tax years 2000 through 2002, the Bureau made the following adjustments to the returns filed by [Redacted]:

<u>Tax Year</u>	2000	2001	2002
Expenses Disallowed	\$53,191	\$ 49,817	\$28,606
Dawson's Downtown Loss		\$ 60,765	
Total Bureau Adjustments	\$53,191	\$110,582	\$28,606

The \$60,765 [Redacted] adjustment was made by the Bureau to remove what it believed to be the items of income and expense associated with another legal entity from the income and expenses that should have been reported as that of [Redacted]. In 2001, the [Redacted][Redacted] formed a "C" corporation but apparently did not for recordkeeping purposes maintain separate records for each of the entities in 2001. The Bureau's adjustments relating to the other entity are discussed in more detail in the Commission's Decision in Docket No. 19041.

The [Redacted] accounts adjusted by the Bureau can be further broken down into the following categories:

<u>Tax Year</u>	2000	2001	2002
Meals	\$ 3,348	\$ 2,341	\$ 2,282
Maintenance/Repairs	388	0	1,195
Travel/Entertainment	5,374	16,680	2,202
Depreciation			3,060
Insurance		1,603	1,727
Contract Labor	37,047	19,851	10,055
Automobile Expense	5,127	5,275	5,168
Building Repairs	300		
Advertising	1,476	1,971	
Supplies	131	1,548	
Office Décor		548	702
Subcontractors			2,215
Total Bureau Adjustments	\$53,191	\$49,817	\$28,606

In reviewing the page two explanation page attached to the July 29, 2005, modified audit report, the Bureau disallowed various expenses for failure to provide sufficient documentation to show that [Redacted] was entitled to the deduction and with respect to those expenses subject to the Internal Revenue Code section 274 heighten documentation requirements (i.e. travel expenses, entertainment expenses, business gifts, and "listed property"), the Bureau argues that [Redacted] failed to maintain the detail documentation as required under that section.

[Redacted]As a result of the disallowance of expenses to [Redacted], the [Redacted]s' Idaho taxable income increased by \$53,191, \$110,582, and \$28,606 for tax years 2000, 2001, and 2002, respectively. Additionally, in 2002, the Bureau identified an \$8,567 difference between what the [Redacted]s reported as compensation from [Redacted] and what was reported as officer's compensation on the return for [Redacted]. Audit increased the amount of 2002 W-2 wages reportable by the [Redacted] by \$8,567.

Finding

This case involves various deductions in computing taxable income. Taxable income in Idaho is based upon federal taxable income, and the principles of federal income tax law generally apply in Idaho. See Idaho Code sections 63-3002, 63-3011B and 63-3022. It is well established in Idaho law, as well as federal income tax law and the tax laws of other states, that a taxpayer claiming a deduction, exemption, or credit bears the burden of establishing his or its entitlement to the same, both as to law and fact. As to law, statutes allowing deductions and exemptions are "construed strongly against the taxpayer."¹ The U.S. Supreme Court has stated:

¹Potlatch Corp. v. Idaho State Tax Com'n, 128 Idaho 387, 913 P.2d 1157, 1159 (1996), *citing* Hecla Mining Co. v. Idaho Tax Com'n, 108 Idaho 147, 151, 697 P.2d 1161, 1165 (1985).

Whether and to what extent deductions shall be allowed depends upon legislative grace; and only as there is clear provision therefor can any particular deduction be allowed. . . . Obviously, therefore, a taxpayer seeking a deduction must be able to point to an applicable statute and show that he comes within its terms.²

If a material fact upon which a deduction depends is not proved, the taxpayer, upon whom the burden rests, must bear his or her misfortune.³

It is the Commission's finding that neither [Redacted] nor the [Redacted] have met their burden of showing the Bureau's adjustments to be incorrect.

WHEREFORE, the Notice of Deficiency Determination issued to [Redacted], dated July 16, 2004, as modified by the Bureau on July 29, 2005, is hereby APPROVED, AFFIRMED, and MADE FINAL.

WHEREFORE, the Notice of Deficiency Determination issued to [Redacted], dated July 16, 2004, as modified by the Bureau on July 29, 2005, is hereby APPROVED, AFFIRMED, and MADE FINAL.

IT IS ORDERED and THIS DOES ORDER that [Redacted][Redacted] pay the following tax and interest:

YEAR	TAX	INTEREST	TOTAL
2000	\$4,205	\$1,500	\$ 5,705
2001	534	150	684
2002	1,421	306	1,727
		TOTAL DUE	<u>\$ 8,116</u>

²New Colonial Ice Co. v. Helvering, 292 U.S. 435, 440 (1934); *see also* Appeal of Sunny Ridge Manor, Inc., 106 Idaho 98, 675 P.2d 813 (1984); Bistline v. Bassett, 47 Idaho 66, 272 P. 696 (1928).

³Burnet v. Houston, 283 U.S. 223 (1931).

Interest is calculated through December 31, 2006, and will continue to accrue at the rate set forth in Idaho Code section 63-3045.

DEMAND for immediate payment of the foregoing amount is hereby made and given.

An explanation of the petitioners' rights to appeal this decision is enclosed with this decision.

DATED this ____ day of _____, 2006.

IDAHO STATE TAX COMMISSION

COMMISSIONER

CERTIFICATE OF SERVICE

I hereby certify that on this ____ day of _____, 2006, a copy of the within and foregoing DECISION was served by sending the same by United States mail, postage prepaid, in an envelope addressed to:

[REDACTED]
[REDACTED]
[REDACTED]

Certified No.
